

# ***Chinese Drywall Risk Management Issues and solutions***

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Chinese drywall will affect thousands of “responsible parties” as the unfortunate owners of contaminated properties search for sources of funds to pay for the remediation of their property. A series of exclusions and limitations in all property and liability insurance policies makes it very unlikely that any of the parties associated with a property that has Chinese drywall installed in it will have any insurance coverage at all for the costs to remediate the property or pay for the injuries to the occupants. One exception to this general rule is fire and water restoration contractors who have good coverage for mold losses may also have coverage for Chinese drywall related losses.

Restoration contractors face two risk management challenges related to Chinese drywall; 1. Drywall installed in routine fire and water damage restoration projects between 2003 - 2008 and 2.) taking on new work to remediate Chinese drywall which was previously installed by another contractor. Many of the newer low cost insurance options offered to restoration contractors have significant coverage defects for Chinese drywall associated claims. If you took advantage of these low cost insurance offerings in the past you may have permanently eliminated your insurance coverage for Chinese drywall associated losses from your past jobs. There are a limited number of insurance tools that can be utilized to fill the historical coverage gap if you have one. If you are performing drywall remediations as a new service you will need to modify your insurance coverage accordingly. In either case it is highly recommended to seek out a qualified insurance consultant to see where you are on coverage for prior acts and prospective operations.

## **The Risks Associated With Chinese Drywall**

In short, some but not all sources of Chinese drywall off-gas sulfur dioxide gas which combines with water vapor to form airborne sulfuric acid within the built environment. Most if not all contaminated drywall was installed in 2006 and 2007 in at least twenty four and as many as forty one states. The source of the sulfide contamination is the gypsum rock in China which was used to manufacture the drywall. The contaminated drywall was imported due to a general shortage of drywall in the US as a result of the hurricane damages in 2006. Most of the Chinese dry wall was used for residential projects. Some imported drywall was private labeled and not all was stamped Made in China. As a result it is difficult to determine which specific properties had Chinese Drywall installed in them within this time period. Restoration contractors may have installed contaminated drywall in their normal fire and water damage restoration work. The jury is literally out on the possible adverse health effects to the occupants of the contaminated buildings; these health affects do not appear to be acute. However it is clear that buildings containing sulfide contaminated drywall, which smells like rotten eggs or burned match's will need to be remediated. Remediation involves removing the drywall, assessing and correcting potential structural damage, and the corrosion of electrical systems, HVAC equipment and the building contents. There are no accepted remediation protocols or standards today for Chinese drywall. Damages from the drywall include remediation costs, diminution of property values, increased fire risk and adverse health effects to the occupants and to remediators. Historical loss exposures can be traced to “responsible parties” including developers, construction managers, general contractors, subcontractors, building products suppliers, distributors and manufacturers. Contractors remediating the drywall also have liability loss exposures and usually have significant gaps in their insurance coverage even if they have purchased Contractors Pollution Liability insurance. Literally tens of thousands of properties and

thousands of responsible parties are affected. Generally loss costs approximate 60% of the building value which presents a huge source of potential new revenue for restoration contractors. Some trial lawyers promote Chinese drywall as the largest construction defect issue in history, affecting 100,000 homes. Contractors remediating these properties should recognize that they are entering a high liability risk environment due to the fact that the property owner probably does not have insurance coverage for the needed work and may look to the remediator as a deep pocket. Strong loss control protocols and excellent insurance coverage is needed for the contractors performing these remediations. Traditional insurance is very likely to have significant coverage gaps for this work and should not be relied upon.

### **Traditional Insurance Coverage for Chinese Drywall Related Losses**

Chinese drywall claims encompass traditional construction defect insurance coverage issues and then superimpose various “pollution” exclusion implications. Construction defect claims introduce a series of complex insurance coverage issues in both property and liability insurance policies. In general, acidic gas will fall within the definition of a “pollutant” in both property and liability insurance policies because it is an “irritant” or “contaminant”. Therefore losses associated with Chinese drywall will be impacted by pollution exclusions in virtually all forms of commercial insurance.

Commercial Property and Homeowners insurance policies fundamentally insure losses from discrete fortuitous loss events that result from accidents and natural disasters. It is usually difficult to obtain coverage for a construction defect on a property insurance policy because the prerequisite “insured cause of loss” is missing to trigger coverage under the policy. Commercial property insurance policies also have pollution exclusions. Therefore property insurance policies will usually deny a Chinese drywall loss because of the absence of an insured peril and the effect of the pollution exclusion. As a result most property owners and their lenders will be left uninsured for the costs to remediate Chinese drywall.

Exclusions in Commercial General Liability insurance policies for “Damages to Your Work” and “Impaired Property” can stand in the way of coverage for a contractor.

All of the stakeholders need modified environmental insurance to be covered for these losses. Unfortunately the vast majority of them will not have appropriate insurance for Chinese drywall related losses even though good quality commercial liability and property coverage was available to them pre-loss. There were no good insurance solutions for homeowners.

### **Environmental Insurance Solutions**

To be insured for Chinese Drywall losses a restoration contractor needs a properly structured Contractors Pollution Liability policy which does not have a Property Damage To Your Work or an Impaired Property exclusion, in addition to a GL policy. Only about 1/3 of the CPL policies sold to restoration contractors today do not have these onerous exclusions. High quality coverage does not necessarily cost more than the more restrictive policy forms. In fact these same exclusions can be problematic in a mold loss so if you have good coverage for mold you probably have good coverage for Chinese drywall. But if you are taking on work to remediate Chinese drywall it is very important you tell your insurance company this because this service falls outside the scope of covered operations in most restoration contractor insurance policies.

For example if the rating page of your General liability policy has you rated as a janitor or a carpet cleaner and you are in fact ripping and tearing out Chinese dry wall you are opening yourself up for the denial of a claim based on a material change in the risk. Appropriate insurance is available for this work. However traditional insurance policies will almost certainly excluded everything associated with Chinese drywall for all of the stake holders. Restoration contractors need to address their loss exposures from prior operations and if they perform Chinese drywall remediation work as a service.

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